The Income 'Revolution'

By Victor Perlo

In Collaboration with

Labor Research Association

ARE THE RICH GETTING POORER AND THE POOR RICHER? THIS STUDY REVEALS THE REAL CLASS DISTRIBUTION OF INCOME IN U.S.

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INTRODUCTION

DR. ARTHUR F. BURNS, Economic Adviser to President Eisenhower, claims that there has been a "social revolution" in the United States. Ex-President Truman, in his final Economic Report to Congress, held that: "The products of our economy are now far better distributed than they used to be."[1]

Actually there are threatening clouds on the economic horizon—rising unemployment, consumers going into debt, farm income declining, small business in difficulties, continued pressure of a huge military budget along with large-scale mergers and high corporation profits. These storm warnings call for corrective action. But none is needed, according to those who talk of an accomplished "social revolution" and of the "tax-poor rich" giving up their Westchester estates. A typical popular expression is that by Will Lissner in a full-page feature in the *New York Times.* He claims the masses of the population have enjoyed "the greatest advance . . . in history," while the upper income groups have suffered a decline in their share of production and in their purchasing power "unmatched for size and persistence."[2]

Sylvia F. Porter, financial editor of the *New York Post,* goes further: "America has gone through an 'income revolution' in the last decade—a financial upheaval that rivals anything ever promised by Lenin or ever preached by Stalin—the top income class of our land has been squeezed down. The bottom income groups have been pulled up."[3]

Of course, such panegyrics have purposes. They aim to divert attention from the danger of depression, from the continuing and unsurpassed war profiteering. They aim to make armaments palatable to the people, as a supposed source of improved living standards. They aim to forestall demands for higher wages and to pave the way for wage reductions. They aim to clear the way for cutting taxes on the

"impoverished" rich, while raising them on the poor—a process which is taking place rapidly under the Eisenhower Administration, as exemplified by the President's 25-point tax program of January 1954.[4]

Utilizing this propaganda, official policy is reverting with increasing frankness to the "trickle-down" approach to economic problems of the Coolidge-Hoover era. If not checked in application, this will result in another economic catastrophe of grave dimensions.

Moreover, talk of an "income revolution" serves the propaganda aims of the "cold war" and McCarthyism. The European capitalist countries are in a state of obvious decay, of glaring contrasts between extreme wealth of a few and worsening poverty of the many. Concurrently, the economies of the Soviet Union and the People's Democracies are advancing rapidly. Therefore U.S. capitalism, as self-appointed "world leader" in the battle against socialism, tries to convince the world that it practices a different kind of capitalism, one without poverty, without rigid social classes.

Various publications have appeared within recent years to advance this line. One is the U.S. Labor Department publication *Fruits of Freedom.* Another is the Brookings Institution study on stock ownership, falsely advertised as showing a very widespread distribution of capital ownership in the economy. And *Fortune* magazine ran a series on the U.S. market, advancing the thesis that practically everybody here is a middle-class consumer.

The most widely publicized work of this sort, and the main authority for such statements as we have cited, is a book by Simon Kuznets of the National Bureau of Economic Research and the University of Pennsylvania, entitled, *Shares of Upper Income Groups in Income and Savings.* Dr. Kuznets and a staff spent 10 years in preparing this book of 725 pages, 126 main tables, numerous appendices, and over 100,000 statistical figures.

This work is formidable and scholarly in appearance—and indeed shows real scholarship within specialized technical limits. But in its impact, it provides the theoretical heavy

artillery for the widespread campaign to give more government aid to the wealthy at the expense of the majority. Despite its "monumental" character, Dr. Kuznets' book is fundamentally unscientific in approach and erroneous in conclusion; just as the policies based on its conclusions can lead only to hardship for the majority and to national economic disaster.

Main Conclusions of Dr. Kuznets

Dr. Kuznets reports that in the 10-year period 1919-28 the top 1% of the population got 13.42% of the personal income, but in the period 1939-48, they received "only" 9.90%,* with most of the drop occurring in the later decade. Similar figures are shown for the top 5% of the population.

In the single year 1948, according to Kuznets, the receipts of the top 1% fell to 8.4% of the total personal income. This, then, is the "revolution." Instead of getting 14 or 15 times as much as the rest of us, the top rich people are getting "only" 9 or 10 times as much as the rest of us. The claim is that in comparison with a factory worker getting $3,000 per year, the investor who owns company stock gets not $45,000, but $30,000 per year.

But even these results, limited as they are, lack validity. Kuznets measured the wrong things, and he measured them wrongly. Correct measurement would show no decline in the share of the top 1% or top 5% of the population. And measurement of the right things would show a marked increase in the control over income and wealth by the top handful who run big business in the United States.

* Kuznets gives all his figures in three "variants," the basic variant, the economic variant, and the disposable income variant. For simplicity, in this booklet references are always to the basic variant unless otherwise specified. The basic variant includes all money income except capital gains and losses. The economic income variant includes, in addition, imputed rent on owner-occupied homes and certain technical adjustments. The disposable income variant includes, in addition to most of the economic income items, capital gains and losses, but excludes, or deducts, personal income tax payments.

What Our Study Shows

The present booklet attempts to expose the claims of an "income revolution," and to prove the reality of increasing concentration of income and economic power in the hands of a tiny minority. Particular attention is devoted to Dr. Kuznets' work, as the prime source of the "income revolution" theory.

Chapter 1 shows the biases in Dr. Kuznets' methods, which lead to underestimation of the incomes of the wealthy, especially in recent years. Dr. Kuznets fails to allow for exaggerated reporting of dependents and income splitting. He fails to allow for income which the wealthy do not report through tax evasion and avoidance. He fails to allow for that part of the income of wealthy stockholders left in the form of undistributed corporation profits.

Chapter 2 presents our independent estimates, which correct, although incompletely, for these main errors. Our estimates show that the actual incomes of the top 1% of the population in 1948 were more than double Dr. Kuznets' figure; and the actual incomes of the top 5% were more than four-fifths above Dr. Kuznets' figure. They show that the top 1% received in 1948, as a minimum, about one-sixth of the income of all individuals, and the top 5% received, as a minimum, roughly one-third of the total income of all individuals. These proportions are similar to those shown for 1929. Thus, these minimum, partial corrections show that the widely publicized "income revolution" simply did not happen.

Chapter 3 analyzes changes in the class distribution of income and savings, which is far more important than the individual distribution to which Dr. Kuznets limits his attention. Statistics presented show that the share of the corporations—and thereby of the class which owns them—increased at the expense of the shares of workers, farmers, and small businessmen. It is further shown that the share of manufacturing workers in production has declined one-fourth since before World War II.

1 CRITIQUE OF KUZNETS' METHODS

Errors in Concept and Scope

Dr. Kuznets' most fundamental error is that he undertakes to deal with the distribution of income by individuals instead of by social classes. Thereby he treats a secondary question, not the main question. In present-day capitalist society, the primary division of income is between the workers who produce and the corporations and individuals who own the enterprises. Limiting attention to a given number of individuals confuses this primary division, and can lead to serious distortions. For example, if a John D. Rockefeller divides his estate among a dozen sons and retainers, this will appear in individual income statistics as a "broadening" of income distribution, even if the share of the Rockefeller clan as a whole is increasing markedly. Moreover, available statistics make it possible to calculate the class distribution of income more accurately than the individual distribution of income.

Another weakness in Dr. Kuznets' approach—acknowledged by the author—is his concentration on the top income group, without examining what happened at the bottom of the income scale. A recent Census report estimates that the lowest 20% of all wage and salary earners not only received a mere 3.4% of all wages and salaries in 1939, but fell to an average of 2.7% of the total in the five postwar years 1947-51.[5] Contrast this with the 8.4% of total income which Dr. Kuznets—very inadequately—allots to the top 1%. Even by this measurement, one person at the top received about three times the combined income of 20 people at the bottom.

More, within the narrow framework of the distribution of individual income, limited to wealthy individuals, Dr. Kuznets made vital errors.

Omission of Undistributed Profits

Dr. Kuznets counted only that part of the stockholder's profits distributed to him in the form of dividends, while omitting the currently larger part accruing to him in the form of undistributed corporate profits. Virtually all industry and finance in this country are carried on through corporations. Incomes of the top 1% included 65% of all dividends reported to the Bureau of Internal Revenue in 1948. In other words, these members of the 1% are the top layer of the capitalist class in the United States. They have the deciding voice in the corporations of America. The mass of profits of the corporations are their profits.

Traditionally, the big capitalist did not use all or most of his dividends and interest for living expenses. A large part went to buy up more stocks and bonds, to increase his investment holdings and hence his future profits. This was still broadly true in the United States during the 1920's.

Since then there has been a drastic change. A larger proportion of dividends are used for living expenses. Most profits are left in the tills of the corporations, to expand the size of the existing companies which are already in the top monopoly group. The big capitalists increase their investment holdings and future profits more in this way than by taking the profits personally and then reinvesting them.

In 1929, corporations paid out, after taxes, $5.8 billion in dividends and retained for reinvestment $2.6 billion of profits, or less than half as much. In 1948 the corporations paid out $7.2 billion in dividends and retained for reinvestment $13.5 billion in profits, or almost twice as much. Kuznets considered only the dividends, which increased around 40%. What he should have considered, to begin with, was the total net profits, after taxes, both distributed and undistributed, which increased from $8.4 billion in 1929 to $20.7 billion in 1948, or almost 150%.[6]

Omission of Unreported Income

Dr. Kuznets' method of measuring individual income receipts provided him with a built-in answer. He measured the incomes of the wealthy as being exactly what they reported on their income tax returns—save for minor technical adjustments. But he measured the incomes of the entire population from another source, from the estimates of the U.S. Department of Commerce. These figures, based on reports of income payments by business enterprises, government, and private individuals, are more or less complete. But the statements of income by wealthy individuals for tax purposes are notoriously incomplete. So Dr. Kuznets compares *part* of what the wealthy receive with *all* of what everybody receives. Thus he understates the income of the wealthy. At the same time he overstates the income of the lower income groups by the same amount, since he obtains their share by subtracting his under-estimate of the income of the wealthy from total income. Thus the error of taking the tax returns of the wealthy at face value is compounded.

So it is clear that the top 1% of the population actually received more than the 8.4% of total income in 1948 estimated by Dr. Kuznets.

But this is not the main point. If Dr. Kuznets had understated the incomes of the wealthy to the same extent in both 1929 and 1948, his most important conclusion would still be valid. The share of the upper income groups would still show a sharp decline since 1929; for example, from 21% to 12% in recent years, instead of from 14% to 8% as shown by Dr. Kuznets.

However, under-reporting of income on a vast scale is something which developed *after* 1929. The proportion of income not shown on tax returns in recent years is several times as great as during the late 1920's. Kuznets' calculation of a declining share of the upper income groups is mainly a calculation of the declining extent to which they report their incomes for tax purposes.

If there had been a real "income revolution," one would

expect its impact to have been most pronounced during the middle and late 1930's, the period of New Deal reforms. However, Kuznets' figures show the share of the upper income groups declining but slightly during this period, with a 1939 percentage higher than that of 1919, although somewhat below the 1928-29 peak.

Most of Kuznets' statistical decline took place during the years of World War II, when, in the words of the late President Roosevelt, "Mr. New Deal" gave way to "Mr. Win-The-War." But if there was no "revolution" after 1939 which would cause a real change in the distribution of income, there was, however, a marked increase in taxation, which caused a statistical change in the distribution of income as Kuznets measures it.

Wartime Rates and Tax Avoidance

Because individual income-tax rates increased, especially since 1939, the wealthy have made it a major business to omit from their tax reports a large part of their incomes. In 1939 the surtax rate for those reaching the upper 1% group (that is, with just enough income to fit into this group) was 5%. By 1945 it was 50%. In 1939 those reaching the upper 5% group paid no surtax. By 1945 they paid 26%. This change in tax rates provided a powerful incentive to avoid tax payments.*

* In technical literature two terms are used, tax *evasion* and tax *avoidance*. The former refers to methods which are clearly illegal. The latter refers to methods which make use of legal loopholes and accountants' ingenuity to escape the danger of prosecution. This distinction is not important for the purposes of this booklet. Therefore the single term, tax avoidance, is used to embrace both forms. Furthermore, there is no attempt to make a complete catalogue of the types of tax avoidance. It is dealt with only where pertinent to showing the extent of the difference between the real incomes accruing to the wealthy, and the incomes reported on their tax returns and accepted by Dr. Kuznets. Thus an important form of tax avoidance, excessive deductions for contributions, medical expenses, etc., is not discussed because it does not affect the accuracy of the incomes reported before these deductions. Again, there is no discussion of tax-exempt interest, a well-known form of tax avoidance, because Dr. Kuznets makes a special calculation to add tax-exempt interest to reported income.

Here is a simple illustration of how tax avoidance increased during World War II. In 1941 there were 26 million federal income tax returns. These returns reported $64.8 billion of income, or 68% of the total personal income in this country as estimated by the U.S. Department of Commerce. By 1945 practically everybody earning any money had to report. There were 50 million returns, or almost twice as many as in 1941. If income were fully reported, it would account for almost all of the personal income in the country. But actually, in 1945, income reported on tax returns amounted to only 70.2% of estimated total personal income, hardly any more, percentagewise, than in 1941.

It is obvious that, to a much greater extent than formerly, people were not reporting their full income on tax returns. The tax avoiders could not have been the new taxpayers. These were almost all wage earners and salaried employees whose taxes were taken out of their paychecks by the employers and paid to the government.

There was no such control over the rich. There was and is no withholding of taxes on dividends, interest, private profits, rent, and capital gains.

Tax legislation during World War II included a serious fraud against the people of the United States. It was agreed in principle that all should contribute to the cost of the war. The contribution of working people was insured by Congress through enactment of the Ruml plan for the withholding of taxes on wages and salaries at the source of payment. But in response to big business pressure, Congress failed to enact a similar measure that would have called for the collection of taxes on dividends and interest at the source of payment, even though this would have been technically much easier than the deduction of taxes on payrolls.

After World War II, tight tax collections from workers were continued, and in recent years the rates were increased,

An effective and rounded description of the ways by which the wealthy avoid taxes, and of the reality of heavy tax burdens on the poor, is contained in the publication of the Union Research and Information Service of San Francisco, *Some Hidden Aspects of the Tax System,* May 1952.

while new loopholes were provided for the wealthy. The practical result is that the real tax system has become more and more "regressive," that is, concentrated on those least able to pay.

Kuznets turns this political scandal upside down, and converts the non-payment of taxes by the wealthy into an alleged proof that the wealthy are losing income. This, in turn, is used by the wealthy to support their stepped-up campaign to reduce further the taxes they are supposed to pay and increase those paid by working people.

The government economist, Dr. Selma Goldsmith, formerly with the National Bureau of Economic Research, estimated the percentages of various types of income not reported on tax returns in 1946 (Table 1).

TABLE 1. PERCENT OF INCOME UNREPORTED BY TYPES, 1946

Income source	*Percent unreported*
Civilian wages and salaries	5
Entrepreneurial income	29
Interest	63
Dividends	24
Rent	55

(SOURCE: National Bureau of Economic Research, *Studies in Income and Wealth,* Vol. 13, New York, 1951, page 302.)

It is precisely the upper-income individuals who receive the major portion of income other than wages and salaries. Kuznets himself estimates that the top 5% of the population receive 77% of all dividends, 38% of all rent income, 42% of all interest payments, and 27% of all entrepreneurial income. (Actually, he underestimates these proportions by a considerable margin.)

The tax expert Randolph E. Paul, formerly with the U.S. Treasury, describes the history of income tax avoidance in the United States: "Tax avoidance is intimately associated with tax rates. Modern avoidance made its debut in 1917 when World War I stepped up individual rates to 67%. . . . But the climate of patriotic opinion was against avoidance

during World War I and it made a slow start. Then rates went down gradually until the top surtax and estate tax rates reached the delightful level of 20% in the twenties and tax avoidance lost much of its flavor and meaning."[7]

During the 1930's, according to Paul, New Deal tax rates led to a general attempt to avoid full payment, but this was restrained by Congress, the courts and the Treasury, which at that time, cracked down on tax avoiders.

The World War II years led to really large-scale avoidance. This was made easier by Congress, when in response to business pressure it opened up tax loopholes while raising tax rates. Paul writes: "Congress listened attentively and the 1942 Act set a record for relief." More relief followed in 1943.[8] "A 90% rate proved to be a powerful stimulant to ingenuity . . . the market had never buzzed with so many schemes as in 1943. Never had the schemes been so bold."[9]

Paul traces the situation through World War II. Large-scale avoidance, beginning during the New Deal period of the 1930's, became greatly accelerated during World War II.

Atomic Age Tax Rackets

Again, since World War II, tax avoidance has increased and entirely new methods have been developed. A whole new industry of accountants, lawyers, and business advisory services has grown up to show the wealthy how to get income without calling it income. Congress has passed revenue laws making it progressively easier to do this. There is nothing secret about it.

Many periodicals, including *Life* and *Business Week,* have carried articles on the rapidly developing methods of tax avoidance. Especially worthy of note is the blindness, or worse, of those who are quite aware of the vast and increasing non-reporting of income by the wealthy, and at the same time accept Kuznets' findings as gospel. Sylvia Porter, as previously quoted, swallowed those findings hook, line and sinker. But here is what she wrote a year later:

> There's nothing wrong in avoiding taxes.
> Everyone who can and who has the know-how is trying to do precisely that—including, I hasten to make clear, me.
> Tax avoidance—entirely legal, entirely justifiable—is being developed to the point of a high art in this country. . . .
> It's a fact of life today. And there's nothing wrong about it.[10]

Miss Porter attributes much of the $9.4 billion budget deficit in the fiscal year 1953 to tax avoidance by wealthy individuals and corporations.

The great majority, hit by pay-as-you-go and by excises at every turn, cannot avoid the heavy tax burden. The wealthy minority can and do avoid taxes on an ever-rising scale. It is indeed a sign of the general moral blindness of our rulers that Miss Porter finds "nothing wrong" in this, and proudly announces her own participation.

A catalogue of the main ways by which the wealthy avoid reporting income for tax purposes is provided by an advertisement widely circulated by Prentice-Hall, Inc. This tells how to get away with murder by buying their $19.50 book, *If You're Broke With* $25,000 (*How Top Executives Increase Their Personal Incomes*):

> The first section covers 14 "personal" expenses that may properly be paid in whole or in part by the company. They cover everything from medical expenses to insurance premiums—vacation costs—club membership—auto expenses—meals—hotel accommodations—expenses incurred in connection with your own home—with your country place. These, and like "personal" expenses, may be shared or paid by the company. And bear in mind that $5,000 of such legitimate expenses paid by the company can mean more than a $10,000 increase in taxable salary.

In short, the executives can receive virtually all of their living expenses—on a luxurious scale—without reporting a cent of it as income. At the same time the corporation reports it not as a distribution of profits, but as a business expense. Profits and high incomes are both hidden; taxes are not paid.

In an academic publication, Thomas H. Sanders, Professor of Accounting at Harvard, gives many examples, such as this: "One company prepared a complete list of its ex-

ecutives, with columns for various types of clubs which might be of interest to executives and company alike, and also for summer and winter vacations. The president, after due consideration and consultation, placed check-marks against those items which he thought should go with each of the jobs listed, and which therefore the company would pay for."[11]

How much big business income is hidden in this way? Sanders reports that several executives cited to him as an appropriate arrangement the one made by Congress for the President of the United States: "In 1948 it increased his salary from $75,000 to $100,000; this would normally increase his net income after taxes by some $9,500. But it also observed that the President is under very great expense, much of which looks like personal expense but is actually incident to his position as President. It therefore increased his tax-free expense allowance to $50,000, plus a tax-free travel allowance up to $40,000."[12]

The majority of businessmen interviewed by Sanders regarded this as "a normal, proper, and necessary thing to do," and hoped that the tax authorities would let them get away with as much. They found it "normal, proper, and necessary," to receive $190,000 in salary, of which only $100,000 is reported for tax purposes, while the use of the remainder is regarded as a business expense.

Section 2 of the Prentice-Hall report deals with profit-sharing, bonus and commission schemes; and how the "proper granting of stock options to the top men can pay off in high figures."

By this last method the official, instead of being paid in cash, is permitted to buy company stock at lower-than-market price. This windfall is not immediately reported as income. When he sells the stock and takes his profit, it is supposedly reported as a capital gain and taxed at half-rate with a maximum of 26%. For high-income receivers capital gains are taxed at less than one-third the rate on other incomes. The 1950 Revenue Act made this method sure-fire. Sanders reports: "Executives quite universally want capital gains since they realize that under the existing tax structure

they can accumulate substantial amounts of capital only by this means."[13]

Dr. Kuznets completely excludes capital gains from his basic variant of the income of the upper 1%.

Section 3 of the Prentice-Hall report says: "Perhaps most important of all are the new *retirement income arrangements* that guarantee the executive $5,000, $10,000, $15,000 or more a year for a specific number of years after he retires." By this means, the increase in a salary for top executives is not paid out and reported as taxable income, but is set aside to provide a later annuity.

In 1951 Charles E. Wilson, then president of General Motors, received $201,200 in straight salary, $365,000 in a bonus payable in cash and stock in five installments, and $17,056 as a company payment into a pension fund. He received a total of $583,256, of which only the straight salary (35% of the total) was wholly reportable as taxable income. This is more or less typical.[14]

In order to cover up the growing use of these methods, the Securities and Exchange Commission has dropped the requirement for companies to report the breakdown of executives' salaries.

Section four of the Prentice-Hall book covers "special methods"—"tax arrangements that can work 'miracles' for men in the $25,000 and up brackets."

Prentice-Hall lists among the corporations that have subscribed to its book General Electric, Republic Steel, International Harvester, Texas Gulf Sulphur, and many others.

Of course, the main thing about all these tax steals is the monstrous robbery of the American people, and the heavier tax burdens put on them to supply the public revenue evaded by the upper crust. But for the moment concern must be centered on the statistical device of failing to take all this unreported income into account in measuring income distribution.

The Rich Are Angels

Dr. Kuznets cannot avoid talking about non-reporting of income.[15] He admits the obvious, that income tax returns do not include a large part of the income paid out to individuals. But he claims that under-reporting is by the poor and not by the wealthy. No evidence is supplied to support this conclusion, merely argument and inference. For example:

> Another ground for *assuming* that under-reporting is largely in the lower brackets is that the new entrants into the tax-return population are here, and they are the ones most likely to understate their income. Likewise, the groups that have been among those notorious for noncompliance, farmers and small entrepreneurs, are the ones whose incomes perhaps rose most during the war. (Emphasis added.)[16]
>
> The audit study . . . warrants the *inference* that such underestimation is within a 5% margin for incomes at the top 1% level, and within a 10% margin for incomes in the 2nd through the 5th percentage bands. (Emphasis added.)[17]

He also "reasonably infers" from "the bits of evidence" that the omissions for the top brackets are "not subject to much more serious biases for these recent years than they are throughout the period."[18]

The evidence Kuznets supplies, true enough, consists of mere bits, simply because he chooses to ignore the gross evidence of massive tax avoidance broadly advertised in big business circulars and in the press. But even the bits he supplies really defeat his point. He presents a summary of a sample audit conducted by the Bureau of Internal Revenue of returns in the over-$7,000 bracket, which more or less corresponds to the upper 5% of the population. Out of each 100 returns in the $7,000-$25,000 range, 63 were found to have errors. Out of 100 returns in the over $25,000 range, 70 to 72 were found to have errors. Furthermore, in 88 cases out of 100, the major error was in the reporting of income. As a result of this audit, the Bureau of Internal Revenue increased tax payments by $543 million net, or 7.2%.

It is from this evidence that Kuznets concludes that under-

reporting in the upper income brackets is trifling. The Bureau of Internal Revenue finds evasion in two-thirds of the tax returns of the rich, and adds 7.2% to their tax bill. It does this despite the fact that the laws are rigged to make almost anything permissible, and despite the fact that the tendency of government officials is to give the benefit of the doubt to the rich.

Tax accountants freely describe the "normal" procedure in these tax audits. The executive claims, for example, that $15,000 which he received was not income, but expenses. The Bureau of Internal Revenue agent sits down with the accountant, and they agree that it will be reasonable to disallow $3,000 of the $15,000 claim, and accept as "legitimate" expenses the remaining $12,000.

It is clear, therefore, that the 7.2% figure for tax avoidance, far from indicating the ceiling on this practice, merely scratches the surface, merely catches the most brazen robberies which go far beyond the legal loopholes and which the rich do not bother to cover up.

Kuznets' claim that the lower income groups are the chief tax evaders is contradicted by the federal government itself. Tax Commissioner Schoeneman, in reporting that during 1950 seven out of 10 tax returns on incomes over $25,000 showed "discrepancies," noted that there is a lower frequency of errors in the lower income brackets.[19]

Other "bits of evidence" adduced by Dr. Kuznets, when analyzed seriously, also contradict his conclusion, but space forbids discussing more of them.

Other Experts on Unreported Income

However, it is appropriate to consider additional evidence contained in other studies of the National Bureau of Economic Research. Dr. Kuznets ignores this evidence.

Take the gross non-reporting of interest, dividends and rent, which he assumes is limited mainly to very small recipients who didn't bother to report their incomes of this type. Dr. Selma Goldsmith, in her National Bureau study apprais-

ing the use of income tax data for estimating income distribution, took up the question of the 63% of interest not reported. She found that only 25% of all interest payments were of the types that might be "distributed in small amounts to a very large number of persons," and that 75% went mainly to large receivers. Therefore, since so much was unreported, she concluded that the large receivers obviously failed to report part of their interest receipts—and actually a large part.[20]

Furthermore, Dr. Goldsmith presents evidence to show that under-reporting of interest and rent income increased between 1941 and 1946. Similarly, she shows that only a tiny part of the non-reporting of entrepreneurial income could have been due to the failure of small proprietors to report. Disregarding this evidence, Kuznets talks about the "notorious" evasions of the small proprietors.

Dr. Goldsmith showed that farm income reported on tax returns for 1945 was only 36% of actual farm income, falling short by almost $7 billion. This was one of the great gaps in income statistics. Who was responsible, the millions of small farmers, as Kuznets alleges, or the handful of rich farmers and corporation executives who go in for side businesses or "overrides," as Charles E. Wilson, Secretary of Defense, termed it in describing some of his miscellaneous ventures?

Again, Kuznets ignores the evidence in other National Bureau publications. Nathan Koffsky and Jeanne Lear, in an article in the Bureau's same *Studies in Income and Wealth*, Vol. 13, analyze the distribution of farm income in 1946. They show that three-fourths of all farmers had net cash incomes of less than $2,000, but that the farmers with net cash incomes of over $7,500, who would fit into Kuznets' upper 5%, had 55.6% of the total net farm income.[21] By comparing this with the distribution of farm incomes reported by farmers to the Bureau of Internal Revenue in 1945 (the only year for which such data are available), as shown in Table 2, one can see readily enough which groups of farmers were holding back.

TABLE 2. INCOME GROUP COMPARISON OF FARMS AND THOSE REPORTING FOR TAX PURPOSES

Net cash farm income group	*Actual number of farms, 1946 (thousands)*	*Number reporting for tax purposes, 1945 (thousands)*
$ 1,000 - $ 2,000	773	763
2,000 - 3,000	393	302
3,000 - 4,000	275	136
4,000 - 5,000	211	68
5,000 - 10,000	334	85
10,000 and over	234	25

(SOURCE: Compiled from Koffsky, work cited, p. 235, and Goldsmith, work cited, p. 321.)

For the small farmers with net cash incomes of $1,000-$2,000 reporting was almost complete. But the really gross differences are at the top. Barely one-tenth of the farmers making $10,000 or over admitted it for tax purposes. To get the entire 234,000 farmers with net incomes of over $10,000, it is necessary to dip down into the $3,000-$4,000 group of tax returns. That is, on the average, they reported not more than 30% to 40% of their incomes.

Thus, it is among the very top farmers in Kuznets' upper crust that one has to look for the lion's share of the $6.7 billion of net farm income not reported to the Bureau of Internal Revenue in 1945.

Increasingly during the postwar years rich "farmers" have actually been huge corporate stockholders and executives who have bought up farms to increase their profits and reduce their taxes. Sanders, in his study of executives' tax dodges, talks of their use of "little outside ventures":

> The most frequently mentioned form of outside venture was the farm. . . . A common reason for acquiring a farm is as a hedge against inflation; but other reasons are for a summer home, a place for the children; and last, but not necessarily least, a money-making business enterprise. . . .
>
> It was commonly asserted that there was not much income in these farm ventures by executives, though it seems clear that a number of them do bring in actual income. The more frequent financial considerations were the opportunity to deduct farm losses on the tax return, and the prospect of capital gains.[22]

In short, the executives use farms to make profits directly and through capital gains, while they reduce taxes by reporting "losses" on their tax returns. Kuznets, by accepting the tax returns at face value, understates the actual incomes of the upper crust both by the phony losses and the unreported profits.

The extent of this use of farms by big businessmen is indicated by figures of the 1950 Census of Agriculture showing 38% of all farm land owned by non-farmers. Of course, some of this is owned by corporation farms, and some by banks and insurance companies. But also much represents the "little outside ventures" of the big executives.

Kuznets does not even mention most of the well-known ways by which the wealthy under-report their real incomes in order to avoid payment of taxes, and he ends up by making no adjustment whatsoever for under-reporting, although he concedes that some under-reporting exists, and (in a footnote, p. 441) that it may be more than before World War II.

A new book by a group of Harvard professors, headed by J. Keith Butters, written when Kuznets' results were already available, implicitly criticizes him for ignoring unreported income.* Interpreting tax data showing an apparent decline in numbers reporting very high incomes, and Dr. Kuznets' results, Prof. Butters and associates comment: "To assume that the high surtax rates of recent years have not stimulated upper income bracket taxpayers to an increased avoidance of these surtaxes would be to underestimate the resourcefulness and ingenuity of the American taxpayer."[28]

Directly on Dr. Kuznets' results, they say: "To the extent

* This book, *Effects of Taxation: Investment by Individuals,* is an important contribution which exposes some of the standard apologetics for the wealthy. It reveals the extreme concentration of ownership of productive property in the hands of a very few individuals, and exposes the myth of widespread stock ownership. It shows that tax laws have not hit the wealthy seriously, that the effective rate of taxation on them is much less than is generally supposed, and that they have plenty of money to invest. The National Association of Manufacturers found it necessary to issue a special blast denouncing the Butters work. Needless to say, this blast received much more publicity than the volume attacked.

that taxes have diverted the activities and investments of top bracket individuals into directions which are excluded from income tax data, Dr. Kuznets' data may overstate the decline in the share of these individuals as compared with the share which would be shown if a complete accounting could be made of the total income of all individuals."[24]

Butters and associates qualify this by saying that "it seems quite unlikely that the overstatement of the decline is so substantial as to destroy the general relationships found by Dr. Kuznets."[25] However, the reason given in a footnote for the qualification is not properly applicable to Kuznets' work: "It should be noted in this connection that avoidance of the income tax structure is by no means limited to upper bracket individuals, and it cannot be taken for granted that the degree of avoidance by upper bracket individuals has increased relative to that of the rest of the population over the past 20 to 25 years."[26]

Since Kuznets used only income tax data to determine the incomes in the upper brackets, and subtracted these from total income (largely excluding tax avoidance) to get the income in the lower brackets, tax avoidance in the lower brackets does not affect his figures. On the contrary, increased tax avoidance in the upper brackets results in Kuznets' ascribing more and more *extra* income to the lower brackets, as he subtracts the increasingly incomplete reported incomes in the upper brackets from total incomes.

It is true that correction for unreported income alone is not sufficient completely to destroy Kuznets' general relationships. But taken together with his other errors, it is sufficient. Dr. Kuznets' failure to make any adjustment for unreported income of the wealthy contradicts the judgment of his outstanding associates in the field.

Dr. Goldsmith, in her paper, *Appraisal of Basic Data Available for Constructing Income Size Distributions,* comes to the conclusion that corrections are necessary to adjust for under-reporting of income in field surveys and income tax returns, and that it is "essential" to adjust separately for each type of income, because of the fact that under-report-

ing is more marked in some types of income than in others.

This paper of Dr. Goldsmith was read and discussed at the April, 1949, meeting of the Conference on Research on Income and Wealth sponsored by the National Bureau of Economic Research. Yet Dr. Kuznets, in a work finally published four years later, completely ignored this documented recommendation.

A survey by Dr. Richard A. Musgrave and associates, published in the *National Tax Journal,* March, 1951, adjusted dividends and rents for under-reporting of income, with marked effect. They did this as a matter of course, in a study not primarily dealing with income distribution, but for which partial income distributions were needed in order to estimate tax burdens. (For further discussion of the Musgrave findings see pp. 34-5, 48-9.)

It is hard to believe that Kuznets was unaware of the consensus of expert opinion in favor of making adjustments for unreported income. If anybody had the financial resources to carry out these adjustments, Kuznets did. Objectively, failure to make such adjustments must be considered unscientific, leading to a false result biased in favor of the wealthy classes.

Treatment of Capital Gains

Dr. Kuznets excludes capital gains from his definition of economic income. This is in accord with standard government personal income statistics. But it is not in accord with economic realities. He does include capital gains in his "disposable income variant." But here he combines it with a larger deduction for income taxes paid, so that none of his variants clearly deals with capital gains as part of income. Moreover, he includes capital gains in such a way as to exaggerate the capital gains of the wealthy in 1929, and underestimate them in recent years, thus making still greater the unreal decline in the share of the wealthy in "disposable income."

What is a capital gain? If a person buys a share of General Motors for $30 and later sells it for $60, he makes a capital

gain of $30. If the buying and selling prices are reversed, he suffers a capital loss of $30. Formal economic theory treats capital gains as accidental, occasional income, not like dividends or interest which are received at regular intervals. It regards capital gains as a change in price, not in "real" income. Using these arguments among others, the Republican Administration in the 1920's reduced the tax rate on capital gains to half that on other income.

Actually, the sharp line of demarcation between capital gains and other forms of income built by formal economics is not valid. Furthermore, regardless of the significance of capital gains in the economy as a whole, the receipt of capital gains by an individual provides him with income just as useful as any other form. The dollar bills are the same as those obtained when the investor cashes in his dividend check.

Therefore, measurement of the income of the wealthy should include their capital gains, whether income is measured before taxes, as in Kuznets' basic variant, or after taxes, as in his disposable income variant.

In including capital gains in the latter variant, Kuznets uses the statistical adjustments to income tax reports made for the National Bureau of Economic Research by Lawrence N. Seltzer of Wayne University in his book, *The Nature and Tax Treatment of Capital Gains and Losses.* But he ignores Seltzer's discussion of the character of capital gains and more recent developments concerning them.

Although capital gains or losses are generally regarded as fortuitous speculative events, Seltzer notes:

> Ordinary business profits often contain large amounts of what are essentially capital gains, while large amounts of so-called capital gains are little or no different from ordinary profits, or arise indirectly from the accumulation of ordinary income.[27]
>
> The fortunes accumulated by Rockefeller, Harriman, Mellon, Guggenheim, Carnegie, Morgan, Baruch and many others were not built primarily through the receipt, saving, and reinvestment of ordinary income, but by "realized" and "unrealized" capital gains. In fact, capital gains have played such an outstanding role in the creation of large fortunes as to suggest that they have been their main source.[28]

Consequently, to measure the income of the wealthy while omitting capital gains is to ignore a decisive element in the accumulation of personal wealth. If that is true in general, it is doubly true for the period during and since World War II. Seltzer writes: "The markedly lower tax rates on capital gains have given many taxpayers a strong incentive both to choose investments likely to yield this type of reward and to contrive to have ordinary income take on its appearance. . . . Many taxpayers have found it possible to convert into technical capital gains various amounts of more or less expected income actually representing personal services, profits, interest, or rents."[29]

Of course, this went on to a certain extent also during the 1920's. But then the rate of tax on ordinary income was mild, and the incentive to qualify for the lower capital gains rate was not so strong as at present. Seltzer speaks of the increasingly widespread use of capital gains devices as professional tax advisers and favorable court decisions create wider knowledge of such possibilities. He estimates that realized net capital gains reached an all-time peak in 1946, 230% as much as at the height of the stock market boom in 1929.[30]

Thus, proper treatment of capital gains would show a much larger amount derived by the upper income groups in recent years than in 1929. But Kuznets shows a smaller amount.*

The figures concern realized capital gains. But Seltzer stresses that many of the capital gains are not realized, and hence not reported on tax returns. Instead, they are passed

* The reason for this is that Kuznets took income tax returns at face value without examining their true meaning. Under the tax laws prevailing in 1929, many wealthy people reported huge capital losses, and consequent big deficits in their net income. Therefore, a proper treatment of capital gains and losses of the upper income groups would subtract these losses from the gains of those wealthy people reporting big gains and hence big total incomes. Kuznets did not do this. He included only the big gains in the share of the upper income groups, while subtracting the big losses from the incomes of the lower income groups. With the tax laws prevailing in war and postwar years, capital losses are spread over a series of years, and big losses in single years are infrequent.

on to heirs without payment of income taxes, or realized in a trick way in order to avoid the tax. As a classic example, Seltzer cites Edsel and Henry Ford, who avoided payment of any income taxes on hundreds of millions of dollars in accumulated profits by passing them on as unrealized capital gains to their heirs.

The Fords have carried this still further, according to the *Wall Street Journal,* in order to avoid paying estate taxes on these tax-free capital gains. The Ford family in 1936 created the Ford Foundation. When Edsel and Henry Ford died, in 1943 and 1947 respectively, they willed their majority stockholdings to the Foundation, thus avoiding all estate taxes. Now the Ford family owns barely 5% of the stock in Ford Motor Co., the Foundation 95%. The 5% has all the voting rights. The Ford family reports as income only the dividends on the 5% personally held. The 95% of the dividends going to the Foundation are tax-free, and are not reported as income, although they are controlled by the Ford family, and used according to their will, just as much as the 5% reported.[31]

The importance of unrealized capital gains has been different at different times. As Seltzer puts it: "The tax treatment in the 'twenties was sufficiently favorable to the upper income groups to be accompanied by the realization of gains on an enormous scale by members of these groups."[32] However, in 1942-46: "Among the many forces that restricted the realization of capital gains, the severe tax treatment probably played some part."[33]

Speculative factors also encouraged realization during the 1920's and discouraged it later, according to Seltzer.

Thus, proper treatment of capital gains should include the unrealized capital gains of the wealthy, as well as those realized and reported on tax returns. If this is done, the effect will be to increase the incomes of the upper groups greatly during recent years, but not in 1929. Kuznets, however, makes no allowance at all for unrealized capital gains. By so doing, he again increases his unreal decline in the shares of the upper income groups.

The question of how to measure the unrealized capital gains of the wealthy will be discussed in Chapter 2.

Extra Dependents and Income Splitting

Kuznets based his estimates not on the number of tax returns in the highest brackets, but on estimates of the number of people covered by these returns. Thus, if there are four people per return, only half as many high-income returns will be included in the upper 1% as if there are two people per return.

Actually, with higher tax rates, the upper income receivers make increased use of claiming dependencies in order to reduce their taxes. True, for very high incomes, the savings through this means are small in comparison with other means of tax avoidance and evasion. But so far as Kuznets' methods are concerned, numbers of dependents have a profound effect.

Census statistics show a steady reduction in the number of persons per household over the past two decades. But Kuznets' estimates show sharp increases in the number of persons per upper income return in two years, 1944 and 1948. This can be seen in Table 3.

What happened in 1944? The tax law was changed to permit the claiming of additional dependents. Kuznets notes this in his text, but makes no adjustment for it in his calculations. What happened in 1948? The tax law was changed to permit additional exemptions for old age and blindness. Again, Kuznets takes note of this in his text, but makes a ridiculously inadequate adjustment for it.

If Kuznets' figure for 1948 were adjusted to a basis comparable with the prewar figures it would show in the top bracket an average of around 2.55 persons per return instead of 3.05. He would have to include the incomes of one-fifth more returns in his top groups to reach 1% or 5% of the population, with a resulting considerable increase in income. (Less than one-fifth, since the added returns would be at the low ends of the top groups.)

TABLE 3. AVERAGE NUMBER OF PERSONS PER RETURN IN HIGHEST INCOME BRACKET* USED BY KUZNETS, SELECTED YEARS, 1926-1948

Year	*Number of persons per adjusted** return*
1926	2.87
1929	2.78
1939	2.70
1943	2.67
1944	2.76
1945	2.74
1946	2.73
1947	*n. a.*
1948	3.05

* $10,000 and over for 1926-1943, $11,000 and over in 1944, $14,000 and over in 1945, $20,000 and over in 1946 and 1948. These different groupings more or less correspond to the rising income status of the top income groups.

** Adjusted to eliminate separate returns of wives and community property returns.

Even more important is the splitting of income among a host of relatives in order to reduce tax liability. When taxes were low, a rich person would often receive his income, and then make gifts to or support a considerable number of relatives and dependents of one sort or another. In the tax returns, the entire income was credited to the one receiver.

Today the very rich man often arranges his affairs so that the dividends and other property incomes are distributed directly to a host of dependents and hangers-on. His control is not seriously affected, but the combined tax payments of the group are sharply reduced. Instead of one very big income, the tax returns will show a number of moderate incomes. Most or all of the income will not appear in Kuznets' "top 1%."

Take, for example, the case of the du Ponts who own 35% of the stock of E. I. du Pont de Nemours & Co. This is divided among 117 family members, including old men, women, and children. Their share of the annual dividends paid by du Pont amounted to $42 million in 1948 (almost $100 million in 1950), in addition to their dividends from other corporations. This exceeds the total amounts of divi-

dends reported in the top three groups of income tax returns. The *Statistics of Income* for 1948 show 11 returns with incomes over $3 million each, with a total of $37 million of dividends received. Clearly many of the 117 du Ponts do not even appear among the very high income groups; and much income is thereby omitted from these groups.

A result of the fragmentation of returns can be seen by a comparison of 1929 and 1948 returns, as given in Table 4.

TABLE 4. DISTRIBUTION OF TAX RETURNS, 1929 AND 1948

Income group	*Number of returns*	
	1929	*1948*
Over $1,000,000	513	149
Over $ 100,000	14,816	16,280
Over $ 10,000	374,032	1,212,285

There were three and a half times as many returns showing over a million dollars in income in 1929 as in 1948. But in the latter year there were more returns showing over $100,000, and three and one-half times as many showing over $10,000 as in 1929. Kuznets excludes most of the returns showing over $10,000 from the upper one percent in 1948. But actually, many of those excluded, and some under $10,000, are really divisions of incomes which properly belong in the upper one percent.

Butters and associates comment: "Trusts enable the family property to be split into a larger number of separate taxable units for income tax purposes, and thereby help to transfer income from high tax brackets to lower brackets. The use of trusts, it should be noted, can be combined with gifts, thereby further increasing the tax advantages. . . ."[34]

They cite an example where under the 1952 tax laws up to 60% or 70% of the income accruing to the trust is saved from taxes. A special study of 753 large estates by the U.S. Treasury Department showed that at least one-fifth of the estates had been transferred before death through gifts, and 45% of the remainder after estate taxes and charity

bequests was transferred through trusts.[35] More than two-thirds of those interviewed with incomes of over $50,000 used trusts, generally involving between 30% and 50% of their property.

A single individual can easily have his income divided into a half dozen or more segments. Proper treatment would attempt to bring the separate small or moderate incomes together into one big income for measuring the share of the upper income groups. But Kuznets does nothing of the sort. Indeed, he treats estates and trusts as if they were separate individuals, instead of mere parts of the sources of income of their beneficiaries.

Liebenberg and Kaitz, two Commerce Department technicians, attempting to adjust income distributions so as to group family units together, found on the basis of tax returns and other data that there were 782,000 families of two or more with incomes of over $10,000 in 1944.[36] Kuznets used without such adjustments the tax return figure of 503,000 families with incomes of over $10,000 in 1944. Clearly, he lost a lot of top group income in this way.

Musgrave and associates, in estimating dividend and rent receipts of the top income group, gave special heed to correction for income splitting. As with unreported income, Dr. Kuznets essentially ignores all of the facts about income splitting, widely publicized in technical and popular literature.

Kuznets' Technique

Dr. Kuznets has an excellent technical reputation. Here he frequently uses techniques which have no scientific justification. This is illustrated by a series of technical adjustments he made in passing from his "basic income variant" to his "economic income variant." (For description see p. 7*n.*) These adjustments are almost wholly technical in character, that is, the required figures are not given in income tax returns. Kuznets estimated them by elaborate and roundabout methods, using admittedly arbitrary assumptions. He could just as well have used completely different methods,

yielding quite different results, or for that matter he could have left out the adjustments altogether.

But there is a system to this. The particular methods chosen add, in an exaggerated way, to the claimed decline in upper income shares. The combined effect is to drop the share of the upper 1% in 1946 by 2.15 percentage points as compared with 1929.

As an example, consider the most important adjustment, that for "unwarranted deductions." These include capital losses and tax exempt interest, but consist mainly of the ordinary deductions for taxes, interest, contributions, etc. Virtually all taxpayers take these deductions, either in detail or according to the standard allowance. But Kuznets makes the fantastic assumption that all of the deductions are concentrated on 10% of the returns in each income class, and that 90% of the returns have no deductions. He admits this is a wholly arbitrary assumption. It is more. It is an obviously wrong assumption.

The result of this wrong assumption is that the 10% of returns are boosted up the income ladder sharply, and the incomes of returns in the top groups unduly increased.

The catch comes with the change in tabulation of tax returns in 1944 to groupings by adjusted gross income instead of net income. Adjusted gross income is before the taxpayer makes his ordinary deductions. So Kuznets simply drops his adjustment altogether. The result is an admittedly "maximum" upward adjustment of 1.25 percentage points in the share of the top 1% in 1929; and no adjustment for 1944 and later years. Hence an essentially fictitious drop of 1.25 points in the share of the top 1% is created.

Treatment of Income Taxes

Kuznets' "disposable income variant" features the deduction of personal income tax payments from the income of the upper brackets. This adjustment greatly increases the extent of his fictitious "decline" in the share of the upper income group. For example, for 1929, it reduces the share

of the upper 1% from 14.65% to 13.57%; while for 1947 it reduces the share of the upper 1% from 8.49% to 5.86%. Much use has been made of the "disposable income variant" in popular presentations of Kuznets' material in an effort to buttress the standard big business propaganda about the allegedly intolerable burden of taxes on the wealthy.

But this procedure gives a false impression of the impact of personal income taxes on the wealthy. The theoretical peak individual income tax rate of 88%, recently on the statute books, was widely assailed as a prohibitive tax. However, this theoretical peak was much higher than the *actual* peak rate. Butters and associates showed that the actual effective tax rate on income in 1946 reached a peak of around 47% on incomes of $100,000, then went no higher, but fluctuated in the range of 40-50%, falling below 40% for the $2-$3 million incomes, and below $30% for the $4-$5 million group.[37]

These computed effective rates are on *reported* incomes; on actual incomes, allowing for hidden income in various forms, they would in reality be much lower. But this is not the main point involved in Kuznets' calculations. What he does is to select *one* tax, the federal individual income tax and no other. If adjustment is to be made for taxes, it should include all taxes, direct and indirect. A tax reduces the individual's purchasing power equally, whether it is a sales tax or an income tax. As is well known, indirect taxes, bearing mainly on the poor, have increased perhaps more than income taxes bearing directly on the wealthy.

Musgrave and associates show that in 1948 the total tax burden on income groups under $7,500 per year was fairly constant, at around 26-27%, while total tax on those with incomes over $7,500 was around 36%.[38] This is a relatively small difference, in comparison with the difference in the federal income tax.

In making their calculation they used a very broad (though not improper) definition of income. They allocate to shareholders part of the *taxes* on *corporation* profits, on the theory that these amounts would have gone to the shareholders in

the absence of such taxes. Correspondingly, they allocate this part of corporation taxes as income to the shareholders, before taking it away as a certain percentage of their incomes. In the more limited definition of income used in the present booklet, corporation taxes are not included in the income of the wealthy, and hence that portion of taxes cannot be deducted from it.

With such a reduction of both income and taxes, the resulting tax burden for the highest income group (as given in the Musgrave study) would be reduced to 29%, or only a trifle higher than that shown for the lower income groups.

This percentage would be further reduced by full allowance for the huge unreported income of the wealthy that escapes taxation. Thus, contrary to Dr. Kuznets and customary propaganda, the actual percentage tax burden on the wealthy is no greater than that on the lower income groups. *The effective share of the top income groups in income after taxes is fully as large as their share before taxes.*

Indeed, it is larger when one considers what happens to the taxes after they are collected. The actual fact of the present situation is that the taxes (taken from all classes) are used almost wholly to the advantage of the wealthy. The piddling spending for welfare purposes, some of which benefits the lower-income groups, has been sharply reduced in recent years. Expenditures to advance political and economic interests of the rich have been enormously increased, and completely dominate the federal budget. If one considers the use of tax revenues to pay for high-profit-creating armament orders, to buy overseas markets and politically fix overseas investment outlets for big U.S. corporations, to repress progressives, the Negro people and the labor movement in the United States, to finance plants built at government expense and turned over to big corporations for their operation—it is clear that today a large (perhaps decisive) part of the income of the wealthy is made possible precisely by government spending of tax revenues. The tax burden on the wealthy is thus not really a burden, but one of their most profitable investments.

2 OUR INDEPENDENT ESTIMATES OF TOP INCOMES

TO GET a more reasonable picture of the shares of the upper groups in income, we have made fresh calculations for the years 1929, 1939, 1945, and 1948, in such a way as to avoid the main pitfalls in Kuznets' method. These calculations have four stages:

1. Calculation of income reported on tax returns by top 1% and top 5% of income receivers.
2. Addition of allowances for unreported income.
3. Addition of upper income groups' share of undistributed corporation profits.
4. Comparison of the resulting total with relevant national income figures.

In making these estimates certain assumptions are necessary since available statistics do not give all the data required for precise calculations at all stages. There is nothing wrong in making assumptions in statistical calculations. *All* statistics involve assumptions. The important question is whether the assumptions are biased, or in accord with reality. In virtually every case, Kuznets' assumptions are grossly biased in the direction of proving his argument that the shares of the upper income groups have been declining. The assumptions made in the present booklet are not biased in the opposite direction. They are attempts at reasonable estimates. On points for which there are very few exact data, we "leaned over backwards."

Our results, which show no particular change from one period to another in the share of the upper income groups, are, therefore, minimum conclusions. More adequate data for completely accurate adjustments would probably show an increasing share for the upper income groups.

The following example contrasts one of Kuznets' assumptions with ours. Dividends not reported on tax returns in

1948 amounted to 13.5% of reported dividends. It is necessary to make an assumption as to the distribution of the unreported dividends as between upper income groups and lower income groups as in Table 5.

TABLE 5. REPORTED DIVIDENDS BY INCOME GROUPS, 1948

	Percent unreported of reported dividends	
Income group	*Kuznets*	*Our estimate*
Upper 1%	0	13.5
Upper 5%	0	13.5
Upper 20%	0	13.5
Lower 80%	105.9*	13.5

* Computed from data contained in Kuznets, Tables 123, 114, 111, 69, and *Statistics of Income for 1948,* Part 1, Preliminary Report, Tables 1 and 6.

Kuznets assumes that the top 20% in income report for tax purposes every cent of dividends received, but that the lower 80% fail to report most of the dividends they receive. Our estimate assumes the same degree of non-reporting at all income levels. The reader may judge which assumption is biased, which is reasonable.

Evaluation of a statistical work requires an appraisal of all the assumptions and methods, taken as a whole. Kuznets uses a series of assumptions all biased in the same direction and successively compounding the error in the final results.

Our study uses assumptions which we believe to be reasonable, if not conservative. There is no uniform error compounded in the final result. However, there are in official statistics known omissions of important parts of the incomes of the wealthy, which this booklet mentions but does not attempt to measure statistically.

The most important factor for which we have made no statistical correction is the effect of income splitting on the reported incomes of the wealthy. As indicated above, this is an item of considerable magnitude. If correction were made for it, there would be a substantial further addition to the calculated share of the upper income groups, especially in recent years.

Our final result, then, shows for the upper income groups less than their full share in total income. Furthermore, these omissions have been increasing. Consequently, the final results do not show the actual upward trend in the income share of the wealthy.

There follows a description of the methods used here to calculate the shares of the upper income groups.

STAGE 1: *Top 1% and 5% Tax Returns*

Kuznets estimated the number of tax returns representing the top 1% of the *population* by estimating the number of individuals represented by each return. As has been shown, he did this in such a way as to count too few returns within the top 1% in the later years. Instead, we have directly calculated the number of tax returns representing the top 1% and 5% of the number of individuals receiving income.* This leaves dependents out of the calculations altogether. It avoids underestimating the share of the upper income groups through taking at face value their inflated reporting of dependents.

This method shows the top 1% reporting roughly 10% more income than was shown by Kuznets for 1948, and 1% more than his figure for 1929.

STAGE 2: *Estimating Unreported Income*

Unreported income of the top income groups was estimated separately for each of the five main types of income —dividends, interest, rent, entrepreneurial (business, professional, and farm) income, and salaries. Except for salaries, the same method was used in each case. Taking dividends,

* For 1929 the number of income receivers used was that estimated by the Brookings Institution in *America's Capacity to Consume.* For 1948 the Census survey figure appearing in its release Series P-60, No. 6 was used, reduced by about 2 million to eliminate small recipients of old age and other social security benefits. The Census Bureau series on numbers of households was used to interpolate for intervening years.

for example, the total of dividends paid to all individuals, as estimated by the U.S. Department of Commerce, was compared with the total reported in income tax statistics. In 1948, for example, the Commerce Department total exceeded that reported on tax returns by 13.5%. Therefore, unreported dividends were 13.5% of the amount of dividends reported on tax returns. This same percentage was taken to apply to the top income groups. This method probably underestimates unreported income, because it fails to allow for the special, well-financed efforts of the wealthy to avoid reporting income.*

The percentage additions for unreported income in 1948 are: dividends, 13.5%, interest 64.7%, rent 88.3%, and entrepreneurial income 63.2%. The adjustments for 1945 are generally larger, but those for the pre-war years considerably smaller, except for entrepreneurial income. The adjustments for 1945 and 1948 are consistent with comparable results of Drs. Goldsmith, Musgrave, and Butters. Actually, the corrections are incomplete, especially for the later years, owing to understatements in the Commerce Department series of rent and entrepreneurial income.

The unreported salaries of executives present a different problem. They take on various forms—payments into pension funds for the credit of executives, huge payments charged off to expenses, stock option schemes, deferred bonus payments, contracts to pay salaries after retirement, and many others. These are not only unreported on income tax returns, they are omitted, or only partly included, in the Commerce Department estimates of salaries and wages.

The National Industrial Conference Board analyzed the way in which top executives were compensated in 97 industries in 1949. For every $1 paid in straight salary, about 12

* For the pre-war years 1929 and 1939 an additional step was necessary. During this period a certain amount of property income went unreported not through evasion or avoidance, but simply because the recipients fell below the minimum incomes required for filing returns. Estimates were made of the amount left out for this reason, so as to determine the residual omitted through evasion and avoidance, and thus comparable with later omissions.

cents was paid into tax-free pension funds, and 40 cents as profit-sharing bonuses which, as a rule, were partly taxable and partly tax-free.[39] For example, in 1948 the General Electric profit-sharing scheme was amended in such a way that since then the executive has had to pay a tax on only half of his bonus. In the General Motors plan a smaller proportion comes out tax-free. Generally the tax-free part of the bonus is set aside toward a pension or other form of compensation to be paid after the executive's retirement.

These comprehensive figures of the National Industrial Conference Board make it clear that at least 12% should be added to reported salaries in the top income brackets to allow for pensions and other forms of tax-free deferred payment.

Professor Sanders gives various figures which throw light on the amount of expense allowances. Common practice in big business firms is to allow fixed expense accounts, for which no vouchers need be submitted, in addition to specified expenses covered by voucher: "One president said that in his industry expense allowances of $10,000 a year were common and $25,000 a year not uncommon." Such huge allowances are permitted by the tax authorities. "It seems to be the practice in tax audits to allow fixed allowances for expenses to pass without challenge to the corporations. . . . But this is one of the practices that vary in different parts of the country and with different tax examiners."[40]

The 1948 contract of the Bendix Home Appliances Corp., with its General Manager, Judson S. Sayre, provides $50,000 per year, plus 2% of profits, plus "all expenses of traveling, entertainment, maintenance, hotel and other incidental expenses while away from his place of residence," plus a flat allowance of $5,000 for expenses in general.[41]

In an article in *Life* entitled "The Expense Account Aristocracy," Ernest Havemann gives as "about standard" for a "substantial steel company" 200 officers and salesmen on expense accounts averaging $5,000 per year.[42]

A New York accountant tells us of two extreme examples from among his clients. One executive draws $100,000 per year in salary and $50,000 per year in expense accounts.

Another draws $200,000 in salary and $4,000 in expense accounts.

While these bits of evidence are not readily translatable into a general average percentage, all of them are consistent with the conclusion that not less than 10% should be added to the nominal salaries of executives for compensation disguised in the form of expense accounts.

The 12% for pensions, plus the 10% for expense accounts, adds up to 22%. No attempt is made at a definite estimate of the other devices for adding to executive salaries. It is conservative, however, to guess that they are sufficient to raise the total added payments to 25% of the taxable salary. This calculation applies to 1948.

The available material indicates that pensions and other forms of deferred compensation, while started during World War II, were expanded rapidly thereafter, and by 1948 were perhaps twice as widespread as in 1945. Sanders claims that the use of expense accounts beyond normal business needs became a significant factor during World War II, reaching a peak in that period and tapering off slightly in subsequent years, only to expand again after the beginning of the Korean war. Taking into account the trends in pensions and expense allowances, 20% becomes a rough estimate of the proper total addition for 1945, comparable with the 25% for 1948. No additions are made for pre-war years. Of course, "swindle sheets" were in existence then too. But the widespread, systematic use of these expense accounts as a means of hiding income is a later development.

The combined percentage additions for unreported income are shown in Table 6.

TABLE 6. PERCENTAGE ADDITIONS FOR UNREPORTED INCOME TO TAX RETURN INCOMES OF TOP GROUPS

Year	*Upper 1%*	*Upper 5%*
1929	17.2	17.8
1939	23.6	20.9
1945	44.8	39.4
1948	40.3	39.1

STAGE 3: *Capital Gains and Undistributed Profits*

As has been seen, Kuznets' method of allowing for capital gains exaggerates the amount of capital gains of the upper income group in 1929, and grossly understates the amount in the more recent postwar years. In particular, he makes no allowance for the fact that recently most of the capital gains in the upper income groups have not been cashed in, and hence have not been reported on tax returns.

During recent years all sorts of devices have been developed for expressing profits in the form of capital gains. Seltzer cites 15 main ways of avoiding taxes by such devices. Of these, one is outstanding: "Probably the most important way in which current income—interest, rents, profits, and wages—is converted into capital gains is through the direct reinvestment of profits by ordinary business corporations."[43]

Thus, the undistributed profits of corporations are essentially a direct capitalization of profits, without their intervening payment as dividends to the stockholders. By including these undistributed profits as part of the real income of the stockholders, we include a major share of capital gains. We include them, without respect to the extent to which each individual cashes in on his capital gains by selling the stock, or passes it on to his heirs.

Since business enterprise, especially large-scale business, is carried out mainly through corporations, the undistributed profits of corporations constitute the main part of all capital gains including capital specially created by setting up corporations for the purpose of converting income into capital gains.

Actually, our method is the same as that suggested by Geoffrey H. Moore, Associate Director of Research of the National Bureau of Economic Research. In a speech of friendly comment on Kuznets' work, he stated:

Because of the lower tax rates on realized capital gains than on ordinary income in the high brackets and because unrealized gains are not subject to tax, one would expect the upper income groups to convert as much as pos-

sible of their ordinary income into realized or unrealized capital gains. . . . In connection with unrealized capital gains, there may have been a tendency . . . to pay out relatively less of profits in dividends and retain more to build up the capital of the company and hence escape personal income taxes on dividends. . . . It is easy . . . to allocate the full amount [of undistributed profits] to the various income groups in proportion to their dividend receipts. . . . The effect is to reduce, but not eliminate, the tendency towards equalization of income between 1929 and 1948.[44]

As with other adjustments, this one is incomplete. It is based on the Commerce Department estimates of undistributed corporate profits. But big corporations, like wealthy individuals, fail to report for tax purposes many billions of profits each year. With the aid of government certificates of necessity, corporations convert literally billions from profits into "depreciation" expense. Mining companies deduct from income over a billion dollars a year as spurious "depletion" charges. All sorts of "special reserves" are set up in order to reduce admitted net profits.*

The Commerce Department estimates make allowances for some of the unreported profits. For example, they include for 1947 an addition of $1,350 million in corporate profits disclosed by Bureau of Internal Revenue audits. However, the Commerce Department comments: "It should be noted that not all returns are audited, and that even in the audited returns there may remain some understatement of profits."[45]

This mild statement, coming from a conservative govern-

* An official report of the Temporary National Economic Committee, entitled *Profits, Productive Activities and New Investment,* estimated that over the period 1909 to 1937, unreported corporate retained profits were large enough to imply a $4.5 billion rather than a $3.5 billion annual average of net corporate profits during the 29-year period. In this report the author showed that of the $94 billion increase in corporate net worth over these years, only $28 billion were accounted for by new stock issues. The remaining $66 billion represented for the most part the market valuation of the increased earning power resulting from the reinvestment of actual (rather than reported) retained profits. In the Labor Research Association study, *Trends in American Capitalism,* it was estimated that over the 35-year period, 1909-1944, similar estimates of actual corporate profits show an average profit rate of 11% instead of the reported 7%. The study concludes that "corporations have on the average understated their profits by more than one-third!"

ment agency, must be regarded as a cautious expression of the gross scandal of unreported corporate profits. At any rate, it should be noted that the Commerce Department, unlike Kuznets, does not hold as sacred the reports of the wealthy to the Internal Revenue Bureau and makes some adjustment for their unreported profits.

A full accounting of undistributed profits, therefore, would show much more additional real income going to the wealthy than is calculated in this study. In addition, our calculations make no allowance for the very sizable capital gains accruing to the wealthy through forms other than the increase in real value of corporate stockholdings. The wealthy get additional capital gains through inflation in value of real estate, oil well royalties, and other properties which they hold as individuals or in partnerships and trust funds.

Thus, the method used here shows only a part (although a major part) of the income accruing to the wealthy through appreciation of capital gains. But the result is more nearly complete, and much more accurate, than Kuznets' figures on the capital gains of the upper income groups.

Undistributed profits were allocated to the top income groups in proportion to their share in dividend receipts. For 1948, which was typical, 64.9% of undistributed profits were allocated to the top 1%, and 83.3% to the top 5%.

STAGE 4: *Summary of Results*

A summary of our income calculations for the upper income groups is shown in Table 7.

Kuznets' "basic variant" shows the upper 1% getting 45.8% more in 1948 than in 1929. Our figures show them getting 123.7% more. Kuznets' "basic variant" shows the upper 5% getting 70.5% more in 1948 than in 1929. Our figures show them getting 140.3% more.

The $35 billion received by the top 1% approximates the combined 1948 incomes of all spending units receiving less than $2,650, or about 45% of the spending units in the country, as shown by the Census Bureau. It comes within a

TABLE 7. INCOME OF TOP INCOME GROUPS

(millions of dollars)

A. Top 1%

Item	*1929*	*1939*	*1945*	*1948*
Reported on tax returns	$11,771	$8,553	$14,704	$18,722
Unreported income	2,028	2,019	6,583	7,548
Share in undistributed profits	1,856	760	2,540	8,751
Total	$15,655	$11,322	$23,827	$35,021
Kuznets' estimate, *Total*	11,632	8,120	14,194	16,964
Difference:				
Amount	4,023	3,202	9,633	18,057
Percent of Kuznets' estimate	34.6	39.5	67.9	106.4

B. Top 5%

Item	*1929*	*1939*	*1945*	*1948*
Reported on tax returns	$21,653	$17,372	$32,131	$39,744
Unreported income	3,852	3,625	12,673	15,559
Share in undistributed profits	2,181	926	3,331	11,232
Total	$27,686	$21,923	$48,135	$66,535
Kuznets' estimate, *Total*	20,929	16,137	28,017	35,689
Difference:				
Amount	6,757	5,786	20,118	30,846
Percent of Kuznets' estimate	32.3	35.9	71.8	86.4

billion dollars of the total wages paid to all production workers in manufacturing industries in 1948.

The $66.5 billion income of the top 5% equals the combined incomes of all spending units receiving less than $4,650, or roughly 78% of the spending units in the country. It is considerably more than the $54 billion combined wages of all wage earners in manufacturing, construction, mining, agriculture, and transportation in 1948.

It remains to compare the shares of the top groups with the income of the entire population. This income of the entire population is defined in various ways. Kuznets starts off with the Commerce Department series of individual income receipts but makes sizable adjustments.

The net effect of his adjustments is to show a faster rate of increase in the income of the entire population, and hence a faster decline in the share of the top income groups.

Musgrave and associates make different adjustments appropriate to their measure of individual income.

Here we attempt to answer the question: What is the share of the upper income groups in the country's production? The government statistical series which attempts to measure the country's production is the national income series. Because of its inclusion of undistributed corporate profits, and exclusion of transfer payments, it is closer to the methods of measurement of the income of the wealthy which we have used.

There has been extensive discussion as to the true measure of the national income, and drastic revisions of the government national income statistics have reflected such discussion. It is not the intention here to engage in a critique of national income statistics. However, certain adjustments are necessary for *technical* reasons. The national income statistics include certain items which are excluded from income tax returns, and vice versa.

We have subtracted from the national income military wages, salaries and supplements; corporation income taxes; imputed interest and rent. We have added government interest payments.

Tax laws permitted the omission from income tax returns of the bulk of military wages and salaries in both 1945 and 1948, when they were most important. Moreover, of all items included in the national income, soldiers' pay is the most dubious, and its inclusion for 1945 would grossly distort downward the apparent share of the upper income groups. Corporation income taxes are properly included in national income; but to include them in the comparison, they must also be included in the before-tax income of the corporation stockholders. This was done by Musgrave and associates. However, we have not included this item in the incomes of the top groups. Hence we must also exclude it from the totals of national income for purposes of comparison.

We omit imputed* interest and rent for the same reason

* Imputed income is income not received in cash, but in the form of services which would otherwise have to be paid for. Thus, the owner of a home is credited with an "imputed" income equal to the rent he would have to pay, less his actual expenses.

as Kuznets, because these items are not included in tax returns, and we have made no adjustment to include them in the income of the wealthy. Government interest payments are excluded from the national income, but included in tax returns, and we have attempted to adjust to include the unreported interest in the incomes of the wealthy. Consequently we must add the total of government interest payments to reported national income for purposes of comparison.

The resulting adjusted national income totals are as follows: 1929, $81,584 million; 1939, $68,278 million; 1945, $145,670 million; 1948, $204,053 million. The shares of the upper income groups in the national income, as adjusted, are given in Table 8.

TABLE 8. PERCENT OF TOP INCOME GROUPS IN ADJUSTED NATIONAL INCOME

Year	*Top 1%*	*Top 5%*
1929	19.2	33.9
1939	16.6	32.1
1945	16.4	33.0
1948	17.2	32.6

Throughout the 20-year period, the share of the top 1% remained steady at about one-sixth of the national income. The share of the top 5% remained steady at about one-third of the national income. The fact that the 1929 figures are slightly higher than those for later years is of no real significance. The extent of fluctuation is within the range of error of statistical estimates in a study of this type. Moreover, upward adjustments to the reported incomes of the upper income groups were incomplete, especially for the later years. Full adjustment would undoubtedly more than eliminate the slight apparent decline between 1929 and 1948. In addition, it must be remembered that 1929 was the peak profit year of the boom of the 1920s. An average figure for that decade would show the shares of the upper income groups no higher than in 1945 or 1948.

Checking Results Against Independent Estimates

Musgrave and associates prepared independent estimates of the share of the upper 5.3% in rent and dividends in 1948. Butters and associates prepared independent estimates of the share of the upper 1% and upper 3% in marketable stockholdings (roughly proportional to dividends) as of 1949. Table 9 compares these results with Kuznets' and with ours.

TABLE 9. PERCENT OF UPPER INCOME GROUPS IN DIVIDENDS AND RENTS, VARIOUS SOURCES, 1948 or 1949

	Upper 1%	*Upper 3%*	*Upper 5%*
Dividends			
Kuznets	53.56	65.64	69.84
Musgrave, *et al.*	....	....	77.9
Butters, *et al.*	65.	75.	....
Our estimates	64.9	....	83.3
Rent			
Kuznets	12.77	....	22.60
Musgrave, *et al.*	....	....	45.0
Our estimates	26.1	....	44.9

(SOURCES: Kuznets, Table 123; Musgrave, work cited, Table 1, p. 11; Butters, work cited, p. 440.)

In each case Kuznets' estimates are far below those of Musgrave and Butters, as well as of ours. Our estimate for the dividend share of the top 1% is virtually identical with that of Butters. Our estimate of the rental share of the upper 5% is virtually identical with that of Musgrave, and both are double Kuznets' estimate. Our estimate of the dividend share of the upper 5% is somewhat higher than Musgrave's, but the difference is less than that between Musgrave's and Kuznets' estimates.

Butters does not give a dividend figure for the upper 5%. But his figure of 75% for the upper 3% is consistent with 79% to 80% for the upper 5%. Moreover, Butters gives a range of figures for the upper 3%, of which 80% is the top level. This would be consistent with an even higher figure than our 83.3% for the upper 5%.

There are no estimates, other than ours, of the share of the top income groups in total income that include a systematic attempt to allow for under-reporting. However, Musgrave and associates present an estimate which allows for under-reporting of some types of income. Musgrave also uses a complete concept of income as we do. Despite the partial nature of Musgrave's corrections, his results are much closer to ours than to Kuznets', as can be seen from Table 10.

TABLE 10. PERCENTAGE SHARE OF TOP 5% IN INCOME (1948)

Kuznets	17.63
Musgrave and associates	28.8*
Our study	32.6

* Applies to top 5.3%. The corresponding share for the top 5% would be 28.2%.

These comparisons all confirm the general validity of our results, and of our conclusion that the share of the upper income groups has not declined, but remains very high.

The point bears repeating that our estimates are incomplete, containing only partial corrections for some of the forms of hidden income of the wealthy. Thus a complete measure could be expected to show a pronounced uptrend in the share of the top brackets in individual income receipts. Concerning the more vital question, the rising share of the capitalist class in national income, there can be no doubt whatsoever.

3 CLASS DISTRIBUTION OF INCOME

THE WHOLE discussion of individual income distribution does not touch on a much more decisive question: What has happened to the *class* distribution of income? What has happened to the relative share of entrenched wealth and monopoly as represented by the corporations? What has happened to the share of the small business man, of the farmer?

And finally, what has happened to the share of the worker, and the extent to which he is exploited by capitalists in general, and by big corporate employers in particular?

These questions are really decisive for determining what is happening fundamentally to the economy. They determine whether there has been, in fact, a "revolution," or whether the position of monopoly capital is stronger than ever. Whether the corporate profits are distributed among 1% or 5% is not so important.

The real seat of ownership and control is much narrower even than the top 1%. Butters and associates estimate that the top one-tenth of one percent own 35% of all stock. The control over the decisive corporations is exercised by still fewer individuals, by a few hundred, or at most a few thousand. What has happened to the share of income effectively controlled by this handful, as compared with that going to other groups in the population?

Table 11 shows the trends in the main kinds of privately produced national income, as indicated by U.S. Department of Commerce figures.

TABLE 11. TRENDS IN NATIONAL INCOME BY CLASS DISTRIBUTION

(Index numbers, 1929=100)

Type of income	*1929*	*1939*	*1945*	*1948*	*1952*
Corporate profits	100.0	65.9	200.8	343.9	404.4
Private wages and salaries	100.0	83.0	181.6	255.8	328.9
Income of unincorporated non-farm enterprises	100.0	85.5	231.9	276.8	339.9
Farm income	100.0	79.5	221.1	311.8	268.3

(SOURCE: U.S. Department of Commerce, *Survey of Current Business,* June, 1952, and May, 1953. All types of income are before income taxes.)

Corporate profits have gone ahead more than any other type of income during the postwar years. Incomes of workers, farmers, small businessmen and professionals have all lagged behind. In 1948 the workers were in the lowest relative position; in 1952, as a result of falling farm prices, farmers were in the lowest relative position.

All this is computed with the year 1929 as a base. That was a year of very high profits, at the peak of the boom. Taking almost any pre-war year as a base would show a still wider spread between corporate profits and other forms of income.

The most reliable way is to consider periods of many years. The Commerce Department figures are available for the 24-year period 1929-1952. These may be broken down into the 12 years 1929-1940, roughly the pre-war period; and the 12 years 1941-1952, roughly the war and postwar period. The figures are given in Table 12.

TABLE 12. PRIVATE NATIONAL INCOME BY TYPE, 1929-1952

(in billions)

Type of income	*1929-40*	*1941-52*	*Ratio of later to earlier period*
Corporate profits	$ 45.4	$ 344.5	7.6
Private wages and salaries	411.4	1,199.0	2.9
Income of unincorporated enterprise	68.4	240.5	3.5
Farm income	47.0	158.5	3.4
Rental income of persons	34.2	79.6	2.3
Net interest	59.8	52.5	0.9

(SOURCE: Same as Table No. 11. Rental figures as revised in *Survey of Current Business,* June, 1953.)

In this table the advance of corporate wealth stands out still more sharply. In the later 12-year period corporate profits were 7.6 times those in the earlier period, as compared with 3.5 times for non-corporate business, 3.4 times for farmers, and 2.9 times for workers and employees.

The smaller increase for rental incomes and the decrease for net interest require comment. Both of these series are rough estimates of the Commerce Department, both involve a mixture of actual payments and imputed items. The war and postwar rental estimates involve very liberal deductions for landlords' expenses. The net interest figures exclude the interest on the government debt, which has multiplied several times. Both of these items include large amounts not derived from the process of production, such as house rental and interest on mortgages and consumer credit. They are

limited to receipts of individuals, as distinct from businesses. Hence they do not fit clearly into the picture of the class distribution of income.

But on the whole, Table 12 indicates clearly the increasing dominance of corporate big business, at the expense of labor and the middle classes.

What then has happened to the rate of exploitation of labor by capital as a whole? To approach this question, private wages and salaries can be compared with the total of all other forms of income which involve ownership of productive property. But first it is necessary to shift from wages and salaries to ownership income that part of the proceeds paid out to capitalists in the form of executives' salaries. For this purpose we use our calculations of the wage and salary income of the top 5% of income receivers. This was calculated for only four years, so the average ratio of the wage and salary income of the top 5% to total private wages and salaries was taken as representative for other years. For the first 12-year period, the top 5% received 22.6% of all private wages and salaries; for the second twelve-year period, 21.2%.

After this transfer, the relationship of private wages and salaries to all kinds of ownership income is given in Table 13.

TABLE 13. COMPARISON OF PRIVATE WAGES AND SALARIES WITH ALL OWNERSHIP INCOME, 1929-1952

(in billions)

	1929-40	*1941-52*
Private wages and salaries*	$318.4	$ 944.8
Ownership income*	347.8	1,129.8
Percent ownership income of wages and salaries	109.2%	119.6%

* Salaries of upper 5% of income receivers included with ownership income, and excluded from wages and salaries.

Thus during the prewar period the owners' share was 109% of the workers' share; but during the war and postwar period the owners' share was almost 120% of the workers' share. The Commerce Department figures do not fully show corporate profits, entrepreneurial income, and rents. They

reflect in various ways and to various degrees the attempts of the onwers to minimize their acknowledged profits. To the extent that this is so, the proportion of owners' income to workers' income is understated.

Thus the rate of exploitation of labor in the United States has increased since before World War II, and is far above 100%.

Relative Position of the Worker

A particularly valuable measure of changing income shares is to measure directly the share of a factory worker in his output. At one time or another, this type of measurement has been made by various official and unofficial sources.

The Economic Report of the President to Congress, January, 1953, examined this question for the period since 1946. It found that during the years 1951-52 productivity per man-hour in the economy as a whole was about 17.5% higher than in 1946, while average real hourly earnings in manufacturing were about 11.5% higher than in 1946. Thus the share of labor declined about 5% in this period of five to six years.

The President's report (page 111) states: "The increases in real disposable personal income in the postwar period have been relatively small. . . . In this connection it is interesting to note . . . that during the period over-all, contrary to the common impression, average hourly earnings in manufacturing, adjusted for consumers' price changes, have not risen faster than the economy's general productivity gains, but instead apparently have lagged significantly."

In various ways, these figures minimize the extent of the decline in labor's share of production. For example, productivity increases in the economy as a whole are compared with increasing wages in manufacturing, while it is known that wages in the economy as a whole lagged behind manufacturing wages. Also, no account is taken of the increased direct tax burden on labor since the beginning of the Korean War.

To show the picture since 1939, the Labor Research Asso-

ciation figures on the relative position of the American factory worker have been brought up to date. These figures were published, through 1946, in *Trends in American Capitalism*. They are here brought up through 1952 with the aid of the cost of living index of the United Electrical, Radio & Machine Workers of America (UE), the most recent labor-published index to take account of the effect of taxes paid by workers, as well as correcting for biases in the consumer price index of the U.S. Bureau of Labor Statistics.

Table 14 shows that between 1939 and 1952 the output per manufacturing worker increased about one-third, while his real annual purchasing power remained practically unchanged. Consequently, the workers' share in production, or "relative position," declined about one-fourth. By 1949, the terminal year of Kuznets' calculations, the workers' share was one-fifth lower than in 1939. During the Korean War years there was a further worsening of his relative position.

Readers may observe with skepticism the figures indicating that real annual purchasing power of workers is no higher than in 1939. However, the figures refer to workers regularly employed at all times. Since, in fact, workers were unemployed a large part of the time in 1939, and suffered little from unemployment in 1952, the figures are consistent with the generally observed fact that workers in recent years have been able to buy more goods than during the depression years. If the figures were presented in terms of all workers, employed and unemployed, they would show a rise in purchasing power, but also a correspondingly increased rise in productivity, so that the final column, presenting the "relative position" of the workers, would be the same.

The UE index does reflect to a certain extent increased requirements for commodities—*e.g.*, increased electricity consumption because of the greater variety of living appliances adapted to electricity; increased consumption of gasoline because of greater distance from home to work. Thus, even though the real wages shown by the UE index are no higher than in 1939, the quantity of commodities purchased by a week's wages are somewhat higher.

Table 14. RELATIVE POSITION OF FACTORY WORKER, 1939-52

Year	Output	Employment	Output per worker	Wages and salaries	Average annual earnings employed workers	Index of prices and taxes	Average real annual earnings	Relative position of worker
1939	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1947	174.0	150.0	116.0	312.3	208.2	219.6	94.8	81.7
1948	177.5	149.1	119.0	336.1	225.4	234.0	96.3	80.9
1949	164.1	136.1	120.6	310.7	228.3	230.7	99.0	82.1
1950	187.4	144.5	129.7	357.0	247.1	242.6	101.9	78.6
1951	205.4	154.1	133.3	414.2	268.8	272.3	98.7	74.0
1952	206.3	153.1	134.7	432.4	282.4	285.5	98.9	73.4

(SOURCES: The data on output and employment are from the 1947 Census of Manufactures for the years 1939 and 1947, and thereafter spliced to the indexes of manufacturing output, employment and payrolls compiled by the Federal Reserve Board. See Census of Manufactures, 1947, "Indexes of Production," table 1 on page 1, and issues of the *Federal Reserve Bulletin*. Price indexes are from *Facts About High Living Costs,* issued by United Electrical, Radio & Machine Workers of America, 1951, p. 14, and subsequent releases through July 1952. Monthly indexes of the BLS are used for 1951 and 1952 to fill in the months not covered by the UE indexes, and to determine annual averages consistent with the UE indexes.)

Table 15. RELATIVE POSITION OF FACTORY WORKER, 1899-1952

Year	Output	Employment	Output per worker	Wages and salaries	Average annual earnings employed workers	Index of prices	Average real purchasing power	Relative position of worker
1899	100	100	100	100	100	100	100	100
1909	158	139	114	169	122	129	94	82
1919	222	191	116	518	271	235	115	99
1929	364	190	192	587	309	232	133	69
1939	373	187	199	490	262	188	139	70
1947	649	281	231	1530	544	413	133	58
1952	669	286	269	2119	741	537	138	51

(SOURCES: The figures in Table 14, showing the trends in the years 1939 through 1952, were used to extend the basic table, based on official Census of Manufactures data and BLS data on price changes which appeared in Labor Research Association's *Trends in American Capitalism*.)

This difference exaggerates the decline in labor's share shown in the table. On the other hand, the production index shown is a conservative one. A considerably more rapid increase in productivity could be shown on the basis of published figures.

These figures on the trend in relative position indicate that the fruits of the cold war rearmament program have been very meager for the worker, even though the gain in his productivity could have permitted an increase in his real living standards of over one-third.

This decline in the relative position of the worker is a long-term movement in evidence throughout the entire history of American capitalism. Table 15 shows that over the past five decades the real earnings of the employed factory worker have increased only by about 38%. But in that same period, according to the same authentic sources, his productivity has risen by nearly 170%. Consequently, over this long period his relative position has declined by almost half.

Share of Upper Income Groups in Savings

The distribution of savings is in some respects even more significant than the distribution of income. For accumulation of savings indicates the ability to obtain and extend control over the economy, and hence over the lives and labor of the people.

Income spent on consumption is not the principal measure of the success of the capitalist. For his prime object is not to consume, but to expand his property, power, and profits. The concentration of savings and wealth in the hands of the small upper crust has always been greater than the concentration of income. If there had been a real "bloodless revolution" in America, it would be reflected, surely, in a declining position of the wealth and savings of the top income groups, and a corresponding increase in the holdings of productive wealth and accumulation of savings of lower income groups.

The title of Kuznets' book indicates his intention to deal

with this question. But he does not really do so. Only one of his eleven chapters is on savings. And this chapter is mainly a rehash of various standard studies of savings, combined with elaborate mathematical calculations whose purpose is unclear and whose results are inconclusive. The only definite statements concern cyclical movements in the savings of the upper income group. But statements as to long-term trends are admittedly limited to "conjectures."[46] The vast newspaper and periodical publicity on Kuznets' study says little or nothing on his results in the field of savings.

Why this timidity? Because even the massive statistical machine of the National Bureau of Economic Research was unable to come up with evidence of any "revolution" in the field of savings.

Consider the findings of the 1950 Survey of Consumer Finances, conducted by the Federal Reserve Board and the Michigan Survey Research Center. These show that in 1948 the highest tenth of income receivers, with 31% of the total income, accounted for 78% of all savings. The lowest 40% of income receivers, with 15% of total income, accounted for *minus* 26% of all savings. That is, they lost property or went into debt by an amount equal to more than one-quarter of all individual savings of the country. In 1949, a year of mild slump, the top tenth accounted for 105% of all savings! This means the remaining nine-tenths, on balance, used up savings or went into debt. Over the four years 1947-1950, the average share of the upper 10% in savings was around 83%.

In its book, *America's Capacity to Consume,* the Brookings Institution estimated that in 1929 the upper 10% of the families, according to income, accounted for 86% of the total savings. The slight difference between 83% in recent years and 86% in 1929 is fully accountable in terms of technical peculiarities in the Brookings measurement.

In short, the top income groups monopolize the country's savings just as much now as during the 1920's.

The top 10% includes many of the middle groups as well as the wealthy: it includes those with incomes as low as

$5,000. What about the share in savings of the real upper crust? Butters and associates estimate that the probable share of the top 1% of income receivers in savings during 1947-50 was between 30% and 35%, and that of the top 5% was between 60% and 65%.[47]

Appropriately, Butters and associates refer to savings as investable funds, that is, funds which can be used to increase control over the economy. However, they refer only to investable funds accumulated by the individual out of individual income.

As already noted, in postwar years this has not been the main source of investment funds. The main source has been the undistributed profits of corporations. During the 1947-50 period the total of individual savings came to $31 billion, while the four-year total of undistributed corporation profits came to $49 billion. These undistributed profits are in effect savings of the stockholders. As previously shown, the top 1%, in terms of income, own around 65% of the stock in corporations. Among them is concentrated the effective ownership of and control over the mass of all undistributed corporate profits.

Averaging their share in undistributed profits and their share in individual savings, it turns out that the top 1% own between 50% and 55% of all savings, individual and corporate combined.

Actually, the concentration of ownership is much more marked than this. The figures refer to the top 1% as a group, but not all in this group are capitalists. There are quite a number of high-income professionals and executives, who do not attempt to accumulate productive capital. Butters and associates estimate that 65%-70% of the total holdings of marketable stock are concentrated in the hands of those with net worth of $250,000 or more, "a relatively small fraction of 1% of the population."[48]

Concentration of control is still more marked. First, because the few very largest of the large stockholders are able to control the operations of a giant corporation with much less than half the ownership of its stock. Second, because

giant corporations control the economic life of the entire country, dominate the economic activities of small business and agriculture, as well as the distribution of war orders and other forms of profitable payments derived from taxation of the general public.

What is the relationship between this extreme concentration of savings and capital and the distribution of income? First, the concentration in savings and ownership of capital is more extreme than the concentration of income. Second, the fact that concentration of savings has not diminished, or has even increased, contradicts again Kuznets' conclusion that the concentration of income has diminished. For if the share of the wealthy in income were *really* reduced, their share in savings would be reduced even more rapidly. Kuznets could find no way to escape this contradiction. All he could do was to blur it over: "One can conjecture, for example, that the recent striking drop in the income shares of the upper groups was accompanied by a marked decline in their share in total savings of individuals. This may well have been the case. But the recent period was one of war impact and postwar recovery, when legal and other pressures produced marked fluctuations in the savings habits of individuals. . . . In the postwar years . . . it is quite possible that the share of upper groups in total savings rose again, perhaps to prewar proportions."[49]

Of course, during World War II, with the mass participation in war bond purchases for patriotic and other reasons, the share of the upper income groups in available savings declined somewhat. But the increased savings of the working people had no permanent significance. It was soon dissipated in spending after the war. The share of the upper income groups in savings returned to normal, not despite a decline in their share of income, *but because there was no decline in their share of income.*

Practical Conclusions

The boom of the 1920's was featured by increasing monopoly power, increased exploitation of labor, and an extremely uneven division of income. Partly because of these facts, the ensuing economic crisis was the most severe in our history. It was used by the monopolies to expropriate farmers and small businessmen, and to speed up labor. Millions faced starvation through the loss of jobs, homes, farms, and businesses.

The people struck back, fought for reforms to curb monopoly power and wealth, to ease their own situation, to save their remaining property, and to get jobs and the necessaries of life. Through their mass movement, they turned the government they elected to the course known as the New Deal, and briefly realized small gains at the expense of corporate wealth.

However, through the recent period of war and war preparations, the monopolies and the overlords of industry and finance have succeeded in undermining these slight reforms. That their political power is greater than ever is quite apparent. We have shown that their economic power is also greater than ever, that the conditions of 1929 are repeated on an exaggerated scale.

This is written at a time of economic decline and substantial unemployment. Because the economic situation is in many ways similar to that of 1929, this may herald a crisis even more catastrophic for the people than that of the 1930's. Also, the international economic situation is undeniably worse than in 1929, making the danger still more grave.

The people of this country have no desire to repeat the experience of the 1930's. They do not want to starve and be evicted before they act. They want to forestall the catastrophe.

The "income revolution" which journalists and officials boast about on the basis of Kuznets' work has not occurred.

But it is needed. It is necessary to cut the share of the top income groups in order to protect the living standards of the rest of the population.

Recently the trade unions have advanced programs to this end. An example is that adopted by the United Automobile Workers (CIO) in December, 1953.

This program called for increased and extended unemployment insurance and social security generally; raising the minimum wage to $1.25 an hour; a fair employment practices law with teeth; and 100% of parity for working farmers. It called for raising federal income tax personal exemptions to $1,000, while closing the multi-billion tax loopholes of the wealthy. It proposed increased federal spending and other government activities to promote two million new homes a year; education and health facilities for all; large-scale public works, featuring river-valley development programs and highways. A debt moratorium for the unemployed was also included, as well as measures to expand international trade.

Other leading unions, either singly or through trade union centers, have endorsed programs along these lines.

True, these programs appear to have no immediate practical effect in Washington, where officials are now concerned with quite different matters. Senator Joseph R. McCarthy and Attorney General Herbert Brownell compete for the "privilege" of crushing the people's rights. The Administration sponsors more far-reaching anti-labor legislation. Secretary of State John Foster Dulles strives for war. And the "Cadillac Cabinet" as a whole opens the Treasury for wholesale looting by the vested interests.

The fact is that war and reaction are closely linked with concentrated economic power, and must be attacked together. A number of independent trade unions have combined their proposals for increased purchasing power with a forthright attack on the war policies of the Administration and unqualified resistance to McCarthyism. These unions suggest that the funds for welfare spending may be obtained through

reduction in the military budget; and that vast new foreign markets would be opened by removing the cold-war barriers to trade with one-third of the world's people.

The movement for peace and against McCarthyism is now spreading to more and more trade unions and public organizations of all kinds. This is central, for war and repression create conditions for economic reaction and against progress. At the same time, extreme concentration of wealth and income give birth to military adventures and fascism. This was recognized in words and action by the late President Franklin D. Roosevelt, and in speeches by ex-President Harry S. Truman. The latter, while himself playing the game of big economic interests, in a major campaign speech pointed out how German bankers, manufacturers and landowners had seized control of the economy and chosen Hitler as a "front man" to advance their interests at the expense of labor and the people of the world. He warned that in the United States "there is a growing—and dangerous—concentration of immense economic power in the hands of just a few men."[50]

To curb and check the monopolies, which have become more powerful with this extreme concentration of wealth and income, is not only vital for the economic welfare and political freedom of the American people, but in this age of the H-bomb it is essential for our very survival.

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